No. 796

In the Supreme Court of the United States

OCTOBER TERM, 1939

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v

UNITED STATES REALTY AND IMPROVEMENT COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The District Court filed no written opinion. It expressed its views and announced its decision in open court (R. 336–339). The opinion of the Circuit Court of Appeals (R. 420) is reported in 108 F. (2d) 794.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered February 2, 1940 (R. 430). The petition for writ of certiorari was filed March 7, 1940, and granted April 1, 1940. The jurisdic-

tion of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether a corporation which has securities outstanding in the hands of the public may institute a proceeding for an arrangement under Chapter XI of the Bankruptcy Act or whether it can reorganize under the Bankruptcy Act only pursuant to the provisions of Chapter X.

2. Whether a petition for an arrangement under Chapter XI should be dismissed when the facts disclose that no fair and equitable plan can be consummated under Chapter XI and that no arrangement can be proposed in good faith.

3. Whether the Securities and Exchange Commission, as an agency charged with the duty of administering the safeguards provided by Congress for public investors in reorganizations under Chapter X, was properly permitted by the District Court to intervene in proceedings instituted under Chapter XI by a publicly-held corporation, for the limited purpose of moving to dismiss those proceedings on the ground that the Debtor could reorganize under the Bankruptcy Act only under Chapter X; and, if so, whether it was entitled to appeal from an adverse order.

STATUTE INVOLVED

Chapters X and XI of the Bankruptcy Act (11 U. S. C. Supp. V, Secs. 501 *et seq.* and 701 *et seq.*)

are involved in this proceeding substantially in their entirety. Because of their length they are not printed as part of this brief, but copies thereof have been filed with the Clerk for the convenience of the Court.

STATEMENT

The Debtor, a New Jersey corporation having its principal place of business in New York City, owns and manages real estate investments (R. 6–7, 103). It has outstanding 900,000 shares of no par stock which are listed on the New York Stock Exchange (R. 134). It has direct liabilities of $5,551,416, of which only $74,916 are current liabilities. The liabilities include two series of publicly held debentures, aggregating $2,339,000, which will mature on January 1, 1944, and a $3,000,000 note, due on August 12, 1939 (R. 375). The two series of debentures are secured solely by a pledge of admittedly valueless stock (R. 211–212, 227, 382); the $3,000,000 note is secured by a first mortgage owned by the Debtor.

In addition to the Debtor's direct liabilities it is liable as a guarantor of first mortgage certificates of Trinity Buildings Corporation of New York (hereinafter called Trinity). All of the capital stock of Trinity is owned by the Debtor (R. 7). Trinity's principal liabilities are notes of $10,442,483 due to the Debtor and first mortgage certificates in the amount of $3,710,500, held by the public (R. 7, 51). These certificates are secured

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by the real estate and buildings which are Trinity's only substantial assets (R. 51, 169). They are guaranteed as to principal, interest, and sinking fund payments by the Debtor. The principal became due on June 1, 1939 (R. 7–8). Both Trinity and the Debtor defaulted in its payment of the certificates, as well as in the payment of an interest installment of $102,038, which became due at the same time (R. 171, 175).

The claimed value of the Debtor's assets is $7,076,515. $5,200,000 is represented by the stock of a subsidiary and a first mortgage on a building owned by the subsidiary; the mortgage is pledged to secure the $3,000,000 note mentioned above. Current assets are less than $400,000. The balance of the claimed assets consists chiefly of mortgages, loans, and other securities in the amount of $555,655; an investment of $477,300 in securities of an independent company; unimproved real estate valued at $290,000; and a note receivable from a subsidiary for $137,500 (R. 375).

Each year since 1936 the Debtor has suffered a net loss, not including interest charges under the guaranty of the Trinity certificates (R. 59).

Prior to the maturity of the Trinity certificates, the Debtor and Trinity jointly proposed a Plan and Arrangement to the certificate holders for the purpose of modifying their respective obligations on the certificates, but which was to leave unaffected the other indebtedness and stock of the Debtor (R. 30, 40–41). The maturity of the cer-

tificates was to be extended, the interest reduced, and the sinking-fund payments modified.[1] The Debtor's guaranty was to be modified to conform to these changes in principal and interest, and its present guaranty of sinking-fund payments was to be eliminated entirely (R. 39).

The Plan and Arrangement was to be consummated by the institution of two proceedings: a proceeding instituted by the Debtor under Chapter XI of the Bankruptcy Act for an arrangement to modify its guaranty of the Trinity certificates, and a subsequent proceeding to be instituted for Trinity in the state courts under the Burchill Act to conform Trinity's primary obligation to the modified guaranty (R. 33–34).[2] The Plan pro-

[1] The maturity of the certificates was to be extended for ten years and one month and the interest was to be reduced from a fixed rate of 5½% per annum to a fixed rate of 3%, with additional interest, if earned, of 1% until July 1, 1944, and thereafter of 2% to maturity, but the additional interest was to be paid at maturity whether or not earned. The sinking-fund obligations of $200,000 per year (R. 22–27) were to be replaced by "if earned" obligations, with permission to use the fund to purchase certificates in the open market without, as at present, first exhausting tenders (R. 35–38).

[2] Debtor's counsel stated that the Debtor desired prior approval of the arrangement by the United States District Court for the "pressure" it would put on the state court before which the Burchill Act proceeding would be brought (R. 277).

The Burchill Act (N. Y. Real Property Law, Secs. 121–123) provides for reorganization of property covered by a trust mortgage, the plan to be binding upon all holders of bonds and certificates unless one-third dissent.

vided, however, that the modification of the Debtor's guaranty in the Chapter XI proceeding was to stand even though the state court should subsequently refuse to confirm the proposed modification of Trinity's obligation (R. 34).

On May 31, 1939, pursuant to this Plan, the present proceeding was commenced by the filing of a petition under Chapter XI, accompanied by a plan of arrangement embodying the proposed modification of the guaranty. Prior to filing the petition, however, the Debtor had solicited the consent of the Trinity certificate holders to the plan; these security holders were asked to execute a single instrument indicating their acceptance of both the arrangement to be proposed under Chapter XI and of the plan to be proposed in the Burchill Act proceeding (R. 65). About 53 percent of the holders of the certificates consented to the arrangement (R. 298).

On July 18, 1939, the Securities and Exchange Commission asked leave to intervene in the proceeding for the purpose of objecting by appropriate motions to the jurisdiction of the court and of appealing in the event that its motions were denied (R. 133–138). The District Court entered an order on July 28, 1939, permitting the Commission to intervene (R. 142–143). The Commission then moved the court to vacate the order approving the Debtor's petition, to dismiss the proceeding, and to deny confirmation of the proposed arrangement

on the grounds: (1) that the court did not have jurisdiction over the proceeding because Chapter XI does not apply to a debtor corporation which has securities outstanding in the hands of the public; and (2) that the proposed arrangement could not properly be confirmed under Chapter XI, because, among other reasons, the purpose of the proceeding was to modify the Debtor's obligation on its guaranty while leaving its stock issue and other obligations unaffected, and because the arrangement was not proposed in good faith (R. 145–146). The District Court, although expressing the view that "the proper course is for the * * * company to reorganize all of * * * its intercompany obligations, and the obligations of its subsidiaries under Chapter X" (R. 347), denied the Commission's motions (R. 149–150) and referred the cause to a referee for further proceedings (R. 151).

The Commission thereupon appealed to the court below both from the order denying its motions and from the order referring the proceeding to a referee (R. 392–393). An appeal was also taken by the Debtor from the order of the District Court permitting the Commission to intervene (R. 394). The court below (Clark, J., dissenting) held: (1) the proceedings were properly brought under Chapter XI because under Section 306 (3) any person who could become a bankrupt under Section 4 of the Act may institute Chapter XI pro-

ceedings. (2) The Commission had no right to intervene in a Chapter XI proceeding, even to object to the jurisdiction of the court, because there was, in contrast to Chapter X, no statutory authority to intervene and a nonpecuniary governmental interest was insufficient; accordingly there was no right to appeal. The court below consequently reversed the order of intervention and dismissed the Commission's appeal (R. 430).[3]

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

(1) In failing to hold that the District Court lacked jurisdiction of the Debtor, as a corporation with publicly held securities, under Chapter XI.

(2) In holding that any corporation which could become a bankrupt may file a petition for an arrangement under Chapter XI.

(3) In failing to hold that the District Court properly permitted the Commission to intervene for the purpose of moving to dismiss the Debtor's petition under Chapter XI, and to appeal.

[3] The judgment of the court below dismisses the appeal (R. 430). The majority of the court, however, ruled upon the merits, concluding (Clark, J., dissenting) that any corporation which can be a bankrupt may file under Chapter XI (R. 422–423). Under these circumstances, a mere reversal of the judgment dismissing the appeal and a remand of the case for consideration on the merits by the court below would grant the petitioner no relief. Consequently, disposition of the case requires consideration of the merits as well as of the standing of the Commission to intervene and appeal.

(4) In reversing the order granting the Commission leave to intervene.

(5) In dismissing the Commission's appeal from the orders denying its motion to dismiss the proceeding and referring the proceeding to a referee for further action.

SUMMARY OF ARGUMENT

I

The District Court had no jurisdiction to entertain respondent's petition under Chapter XI because Chapter X is the exclusive method by which corporations with securities outstanding in the hands of the public may reorganize under the Bankruptcy Act. Although literal construction of the definition provisions of the Act would permit a publicly held corporation to file under Chapter XI, the structure of the Act as a whole as well as its legislative history shows unmistakably that such literal construction does not reflect the meaning of Congress. The rule is firmly established that the real purpose and intent of the legislative body must prevail over the literal import of the words used.

Chapters X and XI embody strikingly different schemes of reorganization. Chapter X provides detailed safeguards designed to protect the interests of public investors; Chapter XI provides merely a rudimentary system of creditor control designed for the corporation which has only trade and commercial creditors. The contrast between

the procedures prescribed makes it plain that Congress intended that all public security holders should have the protection afforded by Chapter X and that Chapter XI should be confined to corporations with only trade and commercial creditors.

This conclusion is confirmed by analysis of the present record which strikingly shows the inadequacy of the procedure prescribed by Chapter XI for a corporation in which there is a public investor interest. It is also confirmed by the legislative history of the statute which demonstrates that in enacting Chapters X and XI Congress had clearly in mind the distinction between a closely held corporation and a corporation with securities outstanding in the hands of the public.

II

The District Court should have dismissed the petition because no "fair and equitable" plan can be consummated in the proceeding and no arrangement can be proposed in good faith. Chapter XI provides only for the modification of unsecured obligations; under this chapter, therefore, alteration of the guaranty on the Trinity certificates must be accomplished without altering the Debtor's large stock issue and probably also without modifying its debentures. Yet the Trinity certificate holders have a claim against the Debtor which must be satisfied before the stockholders receive anything and which ranks on a par with that of the debenture holders, since the security behind the debentures is valueless. No plan which modified the

Debtor's obligation on the guaranty but left the stockholders and perhaps also the debenture holders unaffected would be "fair and equitable" as required by Section 366 (3); yet such a plan is the only one which could be consummated under Chapter XI. A disclosure that a plan cannot be consummated in the proceeding goes to the jurisdiction and requires dismissal.

Moreover, under the circumstances presented in this case no arrangement proposed can meet the requirement of "good faith" contained in Section 366 (5). And, even apart from the "good faith" provision, the District Court should have dismissed the proceeding on the ground that the procedure prescribed by Chapter X was more appropriate.

III

The holding of the court below that the District Court should not have permitted the Commission to intervene in the proceeding is clearly erroneous. In effect, the decision establishes the principle that, in the absence of express statutory provision, a governmental agency may never intervene to protect the public from evasion or emasculation of the statute under which the agency functions, unless the agency has some property or pecuniary right affected by the litigation. This drastic restriction upon the power of the Government to protect the public interest finds no support in precedent or policy.

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The interest of the Commission in the present proceeding is twofold. First, as the agency designated by Congress to participate in Chapter X proceedings on behalf of public investors, it has a very real interest in assuring that such investors are not deprived of the safeguards contained in Chapter X through improper exercise of jurisdiction under Chapter XI. Second, it has an equally great interest in protecting its own functions under Chapter X from impairment through improper resort to Chapter XI by corporations which should file under Chapter X. The applicable decisions of this Court clearly establish that this interest is sufficient to support the District Court's order permitting the Commission to intervene.

If the District Court properly exercised its discretion in permitting the Commission to intervene, the Commission had the right to appeal from the orders denying its motion. An interest sufficient to warrant intervention is plainly sufficient to warrant appeal, after intervention, from a decision adverse to that interest.

ARGUMENT

I

CHAPTER X IS THE EXCLUSIVE METHOD BY WHICH CORPORATIONS WITH SECURITIES OUTSTANDING IN THE HANDS OF THE PUBLIC MAY REORGANIZE UNDER THE BANKRUPTCY ACT

The court below, in holding that the respondent had properly filed its petition under Chapter XI,

read the statute with literal exactness but without regard to the Congressional intention. Section 322 provides that a "debtor" may file a petition under Chapter XI, and Section 306 (3) provides that "debtor" means a person who could become a bankrupt under Section 4. Since the respondent could become a bankrupt under Section 4, the two sections, construed literally and without regard to the purposes sought to be achieved by the statute, permitted the procedure adopted.

This literal construction of the Act is, however, contrary to its plain meaning; as we point out below, the structure of the statute as a whole, as well as its legislative history, points unmistakably to the conclusion that Congress intended Chapter X proceedings to be the exclusive method by which corporations with securities outstanding in the hands of the public can reorganize in bankruptcy. Under this interpretation of the Act, the District Court had no jurisdiction over the proceedings instituted by the Debtor under Chapter XI.[4]

Admittedly, in the usual case, it is presumed that the language of a statute expresses the intention of Congress in enacting it. But where, as here, there can be no reasonable doubt that adherence to the strict letter of the law would nullify rather than effectuate the intent of Congress, the presumption is overcome and the clear purpose of Congress

[4] In *In re Reo Motor Car Co.*, 30 F. Supp. 785 (E. D. Mich.), the court held that a corporation which has securi-

must be given effect. *Church of the Holy Trinity* v. *United States*, 143 U. S. 457; *American Security Co.* v. *District of Columbia*, 224 U. S. 491. See also *Keifer & Keifer* v. *Reconstruction Finance Corp.*, 306 U. S. 381, 391; *United States* v. *Ryan*, 284 U. S. 167; *United States* v. *Katz*, 271 U. S. 354; *United States* v. *Jin Fuey Moy*, 241 U. S. 394; *Lau Ow Bew* v. *United States*, 144 U. S. 47. "It is a familiar rule," this Court said in the *Church of the Holy Trinity* case, "that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit, nor within the intention of its makers" (143 U. S. at 459).

The principle that the real purpose and intent of the legislative body must prevail over the literal import of the words employed is particularly applicable in the case of a statute as complex as the Bankruptcy Act. This Court, in *Helvering* v. *Morgan's, Inc.*, 293 U. S. 121, 126, pointedly

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ties outstanding in the hands of the public may not file a petition under Chapter XI. This holding was made in connection with a motion to dismiss a Chapter X proceeding which was based on the asserted availability of Chapter XI. The same result was reached, without opinion, by the District Court for the Southern District of New York in *In re McKesson & Robbins*, No. 72697, decided December 27, 1938, a reorganization proceeding under Chapter X, although certain other factors were there present. *In re Credit Service, Inc.*, 30 F. Supp. 878 (D. Md.), is, however, in accord with the decision below.

observed, with reference to the income tax law, that:

> * * * the true meaning of a single section of a statute in a setting as complex as that of the revenue acts, however precise its language, cannot be ascertained if it be considered apart from related sections, or if the mind be isolated from the history of the income tax legislation of which it is an integral part. * * *[5]

It is, of course, true that in any particular case it is a matter of judgment whether the provisions of the Act and their legislative background do clearly reveal a Congressional purpose at variance with the strict letter of the law. See, e. g., *Palmer* v. *Massachusetts*, 308 U. S. 79, 83; *United States* v. *Missouri Pacific R. R. Co.*, 278 U. S. 269, 277–278; *Wallace* v. *Cutten*, 298 U. S. 229.[6] Here, however, such a variance is established by the very fabric of the Act and by every extrinsic guide to its interpretation; under the authorities above cited, therefore, the will of Congress, even though imperfectly

[5] See also *Duparquet Huot & Moneuse Co.* v. *Evans*, 297 U. S. 216, 218, where the Court said of the Bankruptcy Act itself: "To fix the meaning of these provisions there is need to keep in view the background of their history. There is need to keep in view also the structure of the statute, and the relation, physical and logical, between its several parts."

[6] There is a clear distinction between a case like that at bar, where the question is which chapter of a remedial statute Congress intended a particular type of company to resort to, and a case like *Iselin* v. *United States*, 270 U. S. 245, 251, where the question was whether a tax statute

expressed, must be recognized and obeyed. See *Keifer & Keifer* v. *Reconstruction Finance Corporation,* 306 U. S. 381, 391, quoting from Mr. Justice Holmes in *Johnson* v. *United States,* 163 Fed. 30, 32 (C. C. A. 1st).

A. THE EVIDENCE OF CONGRESSIONAL INTENT WITHIN THE PROVISIONS OF THE STATUTE

1. Chapters X and XI were enacted in 1938 as part of a general revision of the Bankruptcy Act. In this revision, specialized types of proceedings were segregated in separate chapters.[7] Chapter X provides a special procedure for the reorganization of corporations; Chapter XI provides for "arrangements" of the unsecured debts of any person

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could be enlarged by construction "so that what was omitted, presumably by inadvertence, may be included within its scope." See also *Wallace* v. *Cutten,* 298 U. S. 229, 237; *Osaka Shosen Line* v. *United States,* 300 U. S. 98, 101. In the present case, the construction for which we contend does not involve an extension of the scope of the statute but merely an exclusion from the remedial provisions of Chapter XI of publicly held corporations to which Congress did not intend the provisions of Chapter XI to apply.

[7] Chapters I–VII were retained for ordinary bankruptcy proceedings and several types of specialized proceedings were provided for in Chapters VIII–XIV. Chapter VIII contains provisions applicable to farm debtors and to railroads; Chapter IX contains provisions applicable to municipal corporations; Chapter X relates to corporate reorganizations; Chapter XI relates to arrangements of unsecured debts; Chapter XII relates to real property arrangements by persons other than corporations; Chapter XIII relates to wage earners' plans; and Chapter XIV relates to Maritime Commission liens.

who could become a bankrupt. The intended scope of each Chapter is indicated by its ancestry. Chapter X replaced Section 77B, which in turn supplanted the equity receivership mechanism, as the normal reorganization procedure for corporations with widely distributed securities. Chapter XI, on the other hand, replaced the "composition" provisions of Sections 12 and 74 [8] as the normal procedure for adjusting the trade obligations of small individual and corporate businesses.[9]

Reflecting the difference in their genesis, the two Chapters embody strikingly different schemes of

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[8] H. Rep. No. 1409, 75th Cong., 1st Sess., p. 50; S. Rep. No. 1916, 75th Cong., 3rd Sess., p. 18.

[9] The composition cases concluded under Section 12 for bankrupts and the composition and extension cases concluded under Section 74 for individuals during the period from 1932 through 1938 involved average liabilities of substantially less than $50,000. Annual Reports of the Attorney General of the United States, 1932 to 1938, Exhibit 3 in each report. While no comprehensive figures are available to permit an accurate comparison of these figures with the size of equity receivership and Section 77B proceedings, a study made by a Senate committee of receiverships filed in the federal courts in California during the period from 1930 to 1933 showed average liabilities of approximately $1,000,000. S. Rep. No. 365, 73rd Cong. 2d Sess., pp. 1–3. There are, of course, sporadic instances of the use of the composition procedure for large corporations. See, e. g., *In re Realty Associates Securities Corporation*, 69 F. (2d) 41 (C. C. A. 2d), certiorari denied, 292 U. S. 628; *In re O'Gara Coal Co.*, 260 Fed. 742 (C. C. A. 7th). But the rarity of such cases, and the inapposite nature of the composition sections, is indicated by the fact that when the need for more efficient reorganization procedure was first recognized by Congress

reorganization. Chapter X establishes comprehensive administrative machinery and protective provisions for the benefit of public investors, resting on the assumption that such investors, dissociated from control or active participation in the management, need impartial and expert administrative assistance in the ascertainment of facts, in the detection of fraud, and in the understanding of complex financial problems.[10] In contrast, Chapter XI establishes a rudimentary system of creditor control, resting on the assumption that the problem of rehabilitating debtors filing petitions under Chapter XI can be substantially settled at a single creditors' meeting.

Thus, except where the liabilities are under $250,000, Chapter X requires the appointment of a disinterested trustee (Secs. 156–158). The trustee is required to make a thorough examination

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in 1934, it based that procedure on the equity receivership rather than upon the composition practice. Report of Counsel to the Special Committee to Investigate Receivership and Bankruptcy Proceedings, S. Doc. No. 268, 74th Cong., 2d Sess., p. 8; S. Doc. No. 65, 72nd Cong., 1st Sess., p. 90; H. Rep. No. 194, 73rd Cong., 1st Sess., *passim*.

[10] This basic assumption underlies all of the federal securities legislation administered by the Commission, of which Chapter X is an integral part. Securities Act of 1933, c. 38, 48 Stat. 74, 15 U. S. C., Secs. 77a–77aa; Securities Exchange Act of 1934, c. 404, 48 Stat. 881, 15 U. S. C., Secs. 78; Public Utility Holding Company Act of 1935, c. 687, 49 Stat. 838, 15 U. S. C. Supp. V, Sec. 79; Trust Indenture Act of 1939, c. 411, 53 Stat. 1149, 15 U. S. C. Supp. V, Secs. 77aaa–77bbbb.

and study of the debtor's financial problems and management (Sec. 167 (3) (5)). He prepares a report thereon, which is sent to security holders with a notice to submit to him proposals for a plan of reorganization (Sec. 167 (5) and (6)). The trustee then formulates a plan, or reports the reasons why a plan cannot be effected (Sec. 169). To preserve for the court freedom to consider the plan on its merits, unhampered by the appearance of an accomplished fact, Section 176 voids consent to a plan obtained prior to its initial approval by the judge.

In recognition of the fact that public investors in the debtor are likely to be widely scattered, Chapter X provides for their mobilization through specific provisions permitting them to act through agents or committees (Sec. 209) and making lists of security holders available (Secs. 163, 165). It provides for compensation of committees and other representatives (Secs. 241–243). It also provides safeguards against abusive practices by such committees. Section 211, for example, requires committees to file statements showing the circumstances surrounding their formation and Section 212 authorizes the court to disregard provisions in authorizations obtained by committees which are unfair or contrary to public policy. The interests of public investors are further safeguarded by the provisions of Section 206 giving indenture trustees the right to be heard on all matters involved.

Chapter X also provides for participation in the proceedings by the Securities and Exchange Commission. If the judge finds that a plan presented is worthy of consideration, he may refer the plan to the Commission for a report, and must do so where the liabilities of the debtor (as in the present case) exceed $3,000,000 (Sec. 172). When the plan is submitted to creditors after approval by the judge, it is accompanied by the report of the Commission and the opinion of the judge (Sec. 175). By this means investors are provided with an expert impartial analysis of the plan and of the debtor's financial condition, in the light of which the plan may be intelligently appraised. In addition, the Commission is authorized to participate generally in the proceedings as a party with the permission of the court, and with the duty to do so upon the request of the court (Sec. 208).

These provisions indicate a clear recognition by Congress of the necessity for improved reorganization machinery in the interests of public investors and for impartial and expert assistance to the district courts in order that they may more readily exercise the "informed, independent judgment" which this Court has recognized to be essential in reorganization cases. *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, 115; *National Surety Co.* v. *Coriell*, 289 U. S. 426, 436. The Congressional reports show plainly that Chapter X was the medium designed to supply these safeguards (H. Rep. No. 1409, 75th Cong., 1st Sess., pp. 43, 44, 47–48;

S. Rep. No. 1916, 75th Cong., 3d Sess., pp. 21, 30, 31).[11]

No comparable safeguards are found in Chapter XI. It provides only a skeleton procedure for the modification of unsecured debts and contains no provision for the modification of secured debts or stock. The debtor files a petition which is accompanied by its proposed arrangement (Secs. 306 (1), 323, 357). Thereafter a meeting of the creditors is called (Sec. 334) at which creditors may elect a creditors' committee (Sec. 338). After acceptance by a majority in number and amount of the unsecured creditors, the proposal becomes effective upon a finding that it complies with the requirements of the statute (Secs. 362–367). In substance, that is all. There are no provisions for an independent study of the debtor's affairs, for making the information so obtained available to the security holders, or for assuring security holders adequate information before they vote upon a plan. No mention whatever is made of indenture trustees or of security-holder committees, other than the creditors' committee, and the court is given no power of control over such committees. And finally, there is no provision for the proposal

[11] See, e. g., House Report at 47–48; "* * * the court will have the benefits of expert and disinterested advice to aid it in the solution of the complicated financial and legal problems involved in the typical large reorganization. This should fill a long felt need and be welcomed by both courts and investors."

of plans by anyone except the debtor, or for the participation in the proceedings of an independent trustee or an advisory agency.[12]

The contrast between the procedures prescribed by these two chapters makes it plain that they were intended to be mutually exclusive. Indeed, this conclusion seems necessarily to follow from the provision of Section 146 (2) that a petition under Chapter X shall not be deemed to be filed in good faith if adequate relief would be obtainable under Chapter XI. Judge Clark pointed this out in his dissenting opinion (R. 426):

> Under § 146 (2) of Chapter X, a petition filed under that Chapter may not be approved if the judge believes that adequate relief would be obtainable under Chapter XI. Had this debtor filed a Chapter X petition, the court would have been compelled to make an affirmative finding that adequate relief could not be obtained under XI. If the initiation of a X proceeding by this debtor would necessarily have led to such a finding, the same finding should be made when, as here, the debtor has filed under XI. The adequacy of relief under XI is clearly the same issue whether it arises in the setting of a Chapter X petition or in the setting of Chapter XI.

[12] A detailed comparison between the provisions of Chapter X and Chapter XI, in tabular form, is contained in the Appendix, pp. 53–55, *infra*.

Since the two chapters are mutually exclusive, the problem is to determine the precise sphere within which each chapter was intended by Congress to operate. Under the decision of the court below, determination of the appropriate chapter depends solely on whether the debtor proposes to modify any of its obligations other than unsecured debts; if it seeks to modify only unsecured obligations, it may resort to Chapter XI, despite the fact that its unsecured obligations are widely held by the public and despite the fact that the proceeding necessarily discriminates against the holders of the unsecured obligations in favor of the debtor's other security holders. The decision thus imputes to Congress the irrational intention of providing safeguards for mortgage bondholders but not for unsecured debenture holders, or for unsecured debenture holders when secured debts are also to be affected but not when the secured debts are to be left untouched. In our view, the obvious intent of Congress was rather that all public security holders should have the protection afforded by Chapter X and that Chapter XI should be confined to corporations with only trade and commercial creditors.

Congress had good reason for prescribing different procedures for corporations with a public investor interest and for corporations without such an investor interest. Trade and commercial creditors are usually relatively few in number and are

in a position to obtain adequate information and to appear effectively in their own interests.[13] Since, in the normal case, such creditors are well equipped to evaluate plans in terms of self-interest and business knowledge, they may safely be left to appraise the infirmities of a proposed arrangement.[14] But public investors, such as the holders of the Trinity mortgage certificates, who are uninformed, unorganized, and widely scattered, are obviously not qualified to make a like appraisal or similarly to protect themselves against impairment of their interests. Yet, under the decision below, the question of whether public investors shall have the protection of the safeguards provided for them by Congress depends solely on the decision of the debtor whether to propose its plan under Chapter XI or under Chapter X.

2. The irrationality of attributing to Congress the intention of allowing publicly held corporations

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[13] Chapter XI provides for the election of a creditors' committee at the first meeting of the creditors (Secs. 334, 338). This is peculiarly a trade creditors' method of handling the problems of financially embarrassed debtors. Only this committee may be compensated out of the estate. *In re Max Fishman, Inc.*, 27 F. Supp. 33 (S. D. N. Y.).

[14] The fact that Section 393a. (2) of Chapter XI provides for an exemption from the registration provisions of the Securities Act of 1933 (15 U. S. C., Sec. 77e) of an offering of securities pursuant to an arrangement does not indicate that Congress intended Chapter XI to be applicable to corporations with a public investor interest, since an offering to a large number of trade and commercial creditors may constitute a public offering which, apart from the exemption, would have to be registered.

to resort to Chapter XI is effectively illustrated by the present record. The Debtor is in an unhappy financial condition. The book value of its assets, as shown by its consolidated balance sheet, shrank from $123,000,000 in 1930 to $26,561,696 on December 31, 1938; on an unconsolidated basis its assets were shown as $23,478,974 (R. 55). This book value, moreover, was greatly in excess of actual value; the Debtor itself revised its balance sheet as of June 1, 1939, to reflect present market and estimated values and as a result of this revision claimed a total value for all of its assets of $7,076,515 (R. 375, 226, 229). The recent history of the Debtor has been one of successive losses.[15] Trinity, too, has operated at a loss, and, even if the proposed modification of its certificates were to be consummated, its earnings would, at least until the end of 1941, be insufficient by about $50,000 a year to meet the fixed interest requirements (R. 177–178, 373). It is admitted that "No improvement in existing

[15] The Debtor's net losses (after interest charges, but not including any interest charges under the guaranty) for 1936, 1937, and 1938 were, respectively, $190,886, $121,771, and $24,526 before depreciation (R. 59). After allowance for depreciation these losses were $205,700, $131,610, and $25,215, respectively (R. 59). Trinity's operations resulted in net losses, after mortgage interest but before depreciation, of $54,757, $20,782, and $51,546 for 1936, 1937, and 1938, respectively (R. 53). After allowances for depreciation these losses were $239,847, $205,748, and $236,055, respectively (R. 53).

conditions or in earnings is expected in the immediate future" (R. 32).

Because the Debtor's petition has been filed under Chapter XI, there has been no thorough or impartial examination of this financial picture. The extent to which improvident management may have combined in the past with unforeseeable economic conditions to produce the Debtor's present condition has not been determined[16] and there is no basis upon which an intelligent independent judgment can be formed as to the company's future prospects. Obviously Congress intended no such result; to the contrary, its plain purpose was that neither the court nor security holders should be required to pass upon or accept a plan of readjustment, such as that here involved, except upon the basis of a business-like investigation. The Trinity mortgage certificate holders should have been specifically informed that the modifications

[16] By sheer chance the District Court discovered that Trinity had borrowed funds from a bank to meet the interest on its mortgage certificates due December 1, 1938, repaying the loan out of the income of the succeeding semi-annual period (R. 342–352). As a result, the Debtor was relieved of liability on the guaranty for the period ended December 1, 1938, while Trinity failed to earn the interest due on June 1, 1939, and defaulted thereon. Such transactions, testified the vice president of the Debtor, were "not with me an unusual procedure" (R. 350). In addition, transactions whereby Trinity became indebted to the Debtor for more than $10,000,000 (R. 170) and the payment by Trinity to the Debtor of $9,489,986 as interest on a note for $8,781,192 (R. 171–172, 231–233) clearly call for independent examination.

proposed in the plan would still leave overburdensome fixed charges; that the conditions which caused the Debtor and Trinity to show net losses over a period of years would not be corrected by the plan; that the estimated earnings of Trinity for the next three years were less annually than the proposed annual fixed charges by almost $50,000; and that continued payment of interest by the Debtor was highly doubtful in view of its net losses and its future prospects. Instead, the Debtor solicited acceptances to its proposed arrangement in advance of the institution of the judicial proceedings and upon the basis of its unconsolidated balance sheet as of December 31, 1938, reflecting book values grossly in excess of the actual values of its assets (R. 30, 55, cf. 375). Such advance solicitation would have been ineffective under Chapter X, and the availability to the court of the assistance of an independent trustee and of the Commission would have made impossible the solicitation of security holders on the basis of a disclosure so inadequate.

Moreover, by resorting to Chapter XI the Debtor proposes to effect what is actually one plan of reorganization by the piece-meal use of courts of two different jurisdictions. Neither the federal court in the Chapter XI proceedings instituted by the Debtor nor the state court in the Burchill Act proceedings to be instituted for Trinity will have jurisdiction over the plan as a whole. In contrast,

under Chapter X, which provides for the filing of a petition for a subsidiary corporation in the same court which approved the petition of the parent corporation (Sec. 129), the federal court would have complete jurisdiction over both the Debtor and its subsidiary.

Thus, concrete application of the provisions of Chapters X and XI to the Debtor confirms the conclusion flowing from analysis of the Act itself, i. e., that Congress could not have intended to permit the procedure approved by the court below. Chapter XI does not contain the machinery necessary to deal adequately with a corporation in which there is a public investor interest for the obvious reason that it was not designed to apply to such a corporation.

B. THE EVIDENCE OF CONGRESSIONAL INTENT CONTAINED IN THE LEGISLATIVE HISTORY OF THE STATUTE

The legislative history of Chapters X and XI also demonstrates that the decision below does not properly reflect the intention of Congress. In 1932 the Solicitor General, in a report on bankruptcy administration transmitted to Congress by the President, recommended that a statutory scheme for the reorganization of corporations be adopted (S. Doc. No. 65, 72d Cong., 1st Sess.). The Solicitor General explained that such a statute was necessary and desirable to save a failing business conducted "by a corporation having securities out-

standing in the hands of the public representing various interests in its property" (*id.* p. 90). Pursuant to this recommendation, Congress in 1934 enacted Section 77B of the Bankruptcy Act (c. 424, 48 Stat. 911, 912).[17]

Experience thereafter showed the need for amendment of Section 77B. A Special Senate Committee to Investigate Receivership and Bankruptcy Proceedings filed with Congress the report of its counsel, showing that Section 77B had been improperly resorted to by small corporations. The report drew a distinction between small privately owned corporations with trade and commercial debts, on the one hand, and large corporations with securities held by the public, on the other hand; it recommended that the former be remitted to the composition procedure in bankruptcy and that Section 77B or its equivalent be reserved for the latter (S. Doc. No. 268, 74th Cong., 2d Sess., pp. 9–10). It stated in part (pp. 13–15):

> There is * * * a clear distinction to be observed between a corporation, the stock of which is privately owned by a small number of persons, and which is indebted to trade creditors, and a corporation the securities of which are in the hands of the public. The problems of the former are not

[17] This report was also considered by Congress in 1938 in connection with the revision of Section 77B which, as revised, became Chapter X (H. Rept. No. 1409, 75th Cong., 1st Sess., p. 2).

shared by the latter; the problems of the latter have no concern with the former.

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* * * * when the stock of a corporation is in the hands of the public, when large numbers of persons in widely scattered areas have purchased it through stock and bond salesmen and dealers, when the stock of such corporation is listed upon exchanges, and traded and otherwise dealt in in large volume, or when a corporation, either with its stock in the hands of the public or the stock privately held, borrows money by the issuance of bonds or other evidence of indebtedness and such bonds are sold to the investing public, situations are presented that require different treatment.

The large number of stockholders of such corporation and equally large number of bondholders scattered over the entire United States, can neither be represented by private counsel nor be expected to be present at meetings. The number is too unwieldy for any simple or private arrangement. It is no small task to get their acquiescence to a plan, however fair; obviously it cannot be prepared by conference or arrangement with them.

* * * * *

For the bankrupt insolvent corporation, not publicly owned or indebted, let us offer composition under section 12 of the Bankruptcy Act; for the others, let us have section 77B.

Relying in part on this report and in part on a study by the Securities and Exchange Commission of the degree of protection afforded to public investors in reorganizations,[18] Congress in 1938 enacted Chapters X and XI. The hearings[19] and reports[20] on the bill so enacted demonstrate what would in any event be obvious, that Congress did not intend these chapters to provide alternative reorganization procedures for the choice of the debtor. They show that in enacting Chapter X the purpose of Congress was to supply an impartial administrative machinery to assist the courts and public investors in the solution of the complex problems which arise in the reorganization of corporations having securities outstanding in the hands of the public; throughout the reports, there is repeated emphasis on "investors," "investor interests," "publicly owned corporations" and like phrases as related to the objectives of Chapter X.

[18] Securities and Exchange Commission Report on the Study and Investigation of the Work, Activities, Personnel, and Functions of Protective and Reorganization Committees. This study and investigation of corporate reorganizations was made by the Commission at the direction of Congress. Securities Exchange Act of 1934, Sec. 211 (15 U. S. C., Sec. 78jj.)

[19] Hearings before the House Committee on the Judiciary on H. R. 8046, 75th Cong., 1st Sess., pp. 36–39, 45–47, 167–199; Hearings before a Subcommittee of the Senate Committee on the Judiciary on H. R. 8046, 75th Cong., 2d Sess., pp. 9–15, 93–101.

[20] H. Rept. No. 1409, 75th Cong., 1st Sess., pp. 37–51; S. Rept. No. 1916, 75th Cong., 3d Sess., pp. 19–31.

House Report, pp. 37–48, adopted in the Senate Report, pp. 2, 18. The same hearings and reports show that in enacting Chapter XI Congress had the entirely different purpose of affording small enterprises, in which there is no public investor interest, a simple system of debt adjustment under the traditional bankruptcy method of direct creditor control.[21]

It would, we submit, be a nullification of the will of Congress, as revealed in this legislative history and as embodied in the provisions of Chapters X

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[21] The express statement of the House Judiciary Committee with respect to Chapter XI indicates this quite plainly (H. Rept. No. 1409, 75th Cong., 1st Sess., pp. 50–51): "Section 12 has been recast; such features of section 74 are incorporated as are deemed of value and the combined sections are made Chapter XI of the Act under the title "Arrangement". * * *. The inclusion of corporations will permit a large number of the *smaller companies* such as are now seeking relief under Section 77B but do not require the complex machinery of that section, to resort to the simpler and less expensive though fully adequate relief afforded by Section 12."

A representative of the National Bankruptcy Conference, which was responsible for the basic draftsmanship of the Act, explained the purpose of Chapter XI as follows, at the hearing before the House Committee on the Judiciary (Hearings on H. R. 8046, 75th Cong., 1st Sess., pp. 45, 46–47): "Subsection 1 [Chapter XI] is no different from the present section 12 which has been with us for years, except that it allows wider rights. A man goes in, who has a little business as a druggist, and wants to make a composition with his creditors. * * * Now, the man that wants to avail himself of the present subsection 12, which is the composition section * * * is interested in making a composition with his merchandise creditors."

and XI, if literal application of the definition provisions were permitted to prevail over what Congress meant in fact to say. In the pungent words of Mr. Justice Holmes, "it is not an adequate discharge of duty for courts to say: We see what you are driving at, but you have not said it, and therefore we shall go on as before." *Johnson* v. *United States,* 163 Fed. 30, 32 (C. C. A. 1st), quoted with approval in *Keifer & Keifer* v. *Reconstruction Finance Corporation,* 306 U. S. 381, 391.

II

The District Court Should Have Dismissed the Petition Because No "Fair and Equitable" Plan for the Debtor Can Be Consummated Under Chapter XI and No Arrangement Can Be Proposed in Good Faith

The District Court lacked jurisdiction over the Debtor under Chapter XI, not only because the Debtor had securities outstanding in the hands of the public but also because, as the record discloses, no "fair and equitable" plan can be consummated in the proceeding and no arrangement can be proposed in good faith.

Section 366 (3) of the Act, which provides that an arangement may not be confirmed unless it is "fair and equitable," makes applicable to Chapter XI proceedings the rules of law enunciated in *Northern Pacific Ry. Co.* v. *Boyd,* 228 U. S. 482. See *Case* v. *Los Angeles Lumber Products Co.,*

Ltd., 308 U. S. 106.[22] No plan for this Debtor under Chapter XI can be fair and equitable, as required by Section 366 (3), because under that chapter only unsecured obligations may be modified. Consequently any modification of the Debtor's guaranty on the Trinity certificates under Chapter XI must be accomplished without altering the Debtor's large stock issue and probably also without altering its debentures, which are technically secured debts. Yet the Trinity certificate holders have a claim against the Debtor which must be satisfied before the stockholders receive anything and which ranks on a par with that of the debenture holders, since the security behind the debentures is valueless. Under the doctrine of the *Boyd* and *Los Angeles Lumber Co.* cases, no plan for the Debtor would be fair and equitable which modified the debtor's obligation on the guaranty but left the stockholders and perhaps also the debenture holders unaffected—yet such a plan is the only one which can be consummated under Chapter XI.

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[22] The respondent's suggestion in its brief in opposition (p. 4, note 2) that the *Los Angeles Lumber Co.* case is applicable only to corporations insolvent in the bankruptcy sense disregards the fact that all plans for all debtors under Chapters X and XI are required to be "fair and equitable." It also disregards the basis of the decision, which is that the debtor's property must first be applied to payment of the claims of creditors in full before stockholders are allowed to participate. There is no ground for any contention that this rule applies only in the case of debtors insolvent in the bankruptcy sense and that the rights of creditors of other debtors are to be less carefully protected.

The Debtor seeks to escape the force of the doctrine of the *Boyd* and *Los Angeles Lumber Co.* cases by urging that it is not applicable to the plan which the Debtor has proposed, since that plan is an "arrangement" rather than a "reorganization". The argument is, in effect, that Congress intended to permit corporations like the Debtor to propose and effectuate in a Chapter XI proceeding a plan which admittedly would not be "fair and equitable" under Chapter X. Plainly, substance cannot thus be subordinated to procedure; a plan, either under Chapter X or under Chapter XI, whether it be termed a "reorganization" plan or an "arrangement," cannot be fair and equitable if it proposes that stockholders, or one class of creditors, are to profit at the expense of another class of creditors. As this Court pointed out in the *Los Angeles Lumber Co.* case, "fair and equitable" are words of art with a definite content and meaning; there is, therefore, no room for the contention that they mean something different when used in Chapter XI than when used in Chapter X.[23]

[23] This does not lead to the conclusion that Chapter XI has no legitimate sphere of operation, or stated otherwise, that the "fair and equitable" requirement makes the provisions of Chapter XI unworkable. As we have pointed out, Chapter XI was intended to be used by individual and small corporate enterprises, in which the going-concern value of the business is normally dependent on its proprietors. In such cases it may be necessary to provide for the retention of an interest in the debtor or its stockholders in order

The majority of the court below expressed the view that these matters should be left for decision until the plan came up for confirmation. The court apparently overlooked the fact that the issue of confirmation was before the District Court (R. 2). But in any event, the Commission's objection is not to the merits of any particular plan proposed, whether it be the original arrangement or any amended proposal which the Debtor may make; its objection is rather that *no* fair and equitable plan for this Debtor can be consummated under Chapter XI. In our view, a showing that no plan can be consummated in the proceeding goes to the jurisdiction and requires dismissal. Cf. *Tennessee Publishing Co.* v. *American Nat. Bank*, 299 U. S. 18; *O'Connor* v. *Mills*, 90 F. (2d) 665 (C. C. A. 8th); *R. L. Witters Associates, Inc.* v. *Elsary Gypsum Co.*, 93 F. (2d) 746, 748–749 (C. C. A. 5th).[24] Any

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to preserve the going-concern value and make reorganization possible. Consequently, if a proposed arrangement would realize at least as much for creditors as would liquidation—and such was generally the test in cases under Section 12 (see, e. g., *Fleischmann & Devine* v. *Saul Wolfson Dry Goods Co.*, 299 Fed. 15 (C. C. A. 5th))—there might be no unfairness in permitting the debtor or its stockholders to retain an interest, for in such cases the full value of the property would be applied to the claims of creditors to the largest extent possible. Cf. Rostow and Cutler, *Competing Systems of Reorganization*, 48 Yale L. J. 1334.

[24] The decision in *John Hancock Mutual Life Ins. Co.* v. *Bartels*, No. 33, present Term, decided December 4, 1939, does not require a contrary conclusion. That case involved Section 75 (s) of the Bankruptcy Act, a form of procedure unrelated to the statutes in issue, not requiring a "fair and

other course must result in needlessly clogging court calendars with litigation predestined to be fruitless. Cf. *Tennessee Publishing Co.* v. *American Nat. Bank, supra.*

Under these circumstances, and particularly in view of the inappropriateness of the remedy sought to be employed by the Debtor, no arrangement proposed can meet the requirement of "good faith" contained in Section 366 (5). The concept of "good faith" as used in the reorganization provisions of the Bankruptcy Act has been broadly construed; the issue raised is "whether or not the relief sought by debtor is within the purpose, intent and spirit of the statute." *In re Northeastern Water Companies, Inc.*, 24 F. Supp. 653, 655 (N. D. N. Y.) Under the comparable "good faith" clause in Section 77B, the courts refused to take jurisdiction where the interests of creditors would be better served in another pending proceeding or where it appeared unreasonable to expect that a plan of reorganization could be effected.[25] In our view the elements which go to the basic lack of

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equitable" plan, and contemplating a three-year moratorium for farm debtors, with a privilege in the debtor to obtain his property at the end of or during the three years by paying the appraised or sale value thereof.

[25] *In re Williamsport Wire Rope Co.*, 10 F. Supp. 481 (M. D. Pa.), appeal dismissed, 78 F. (2d) 1023 (C. C. A. 3d); *Provident Mutual Life Ins. Co.* v. *University Evangelical Lutheran Church*, 90 F. (2d) 992 (C. C. A. 9th); *In re Tennessee Publishing Co.*, 81 F. (2d) 463 (C. C. A. 6th), affirmed on other grounds, 299 U. S. 18; *Manati Sugar Co.* v. *Mock*, 75 F. (2d) 284 (C. C. A. 2d).

jurisdiction over this Debtor in a Chapter XI proceeding, and which should lead to dismissal for that reason, lead also to the conclusion that the proceeding should be dismissed for lack of "good faith."[26]

Furthermore, even apart from the "good faith" provision, the bankruptcy court had ample power to dismiss the proceeding on the ground that another procedure was more desirable; its failure to exercise this power was, we submit, an abuse of discretion. In an analogous situation, this Court held that a district court abused its discretion in not dismissing an equity receivership proceeding for a building and loan association over which it had jurisdiction where the public interest made it preferable that the liquidation procedure provided by state law be followed. *Pennsylvania* v. *Williams,* 294 U. S. 176. Compare *Thompson* v. *Magnolia Petroleum Co.,* No. 481, present Term, decided March 25, 1940; *General American Tank Car Corp.* v. *El Dorado Terminal Co.,* No. 129, present Term, decided January 2, 1940. Similarly, several district courts undertook to exclude from Section 77B small corporations which were literally within its terms because the procedure provided by Section 12 was deemed to be more appropriate.[27]

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[26] This Court recently reemphasized the requirement of fair dealing between those who control corporations, on the one hand, and the creditors and stockholders of the corporation, on the other hand, not only with respect to the conduct of business dealings but also with respect to the use of legal procedures. *Pepper* v. *Litton,* No. 39, present Term, decided December 4, 1939.

[27] See, e. g., Rule 77B–2 (i) of the District Court for the Southern District of New York. The principle underlying

This case presents the precise converse of that situation and a similar rule should be applied.[28] The rule is peculiarly apposite here where the assumption of jurisdiction by the District Court was in derogation of the policy of Congress and of the public interest.

III

THE COMMISSION WAS PROPERLY PERMITTED TO INTERVENE FOR THE PURPOSE OF OBJECTING TO THE JURISDICTION OF THE DISTRICT COURT AND COULD APPEAL FROM AN ADVERSE DECISION

1. The holding of the court below that the District Court should not have permitted the Commis-

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this rule is now embodied in Sections 130 (7) and 146 (2) of Chapter X which require that every petition under Chapter X shall allege the specific facts showing the need for relief under that chapter and why adequate relief cannot be obtained under Chapter XI, and which require dismissal for lack of "good faith" when such a showing is not made.

[28] Cf. Rostow and Cutler, *Competing Systems of Corporate Reorganization*, 48 Yale L. J. 1334, 1366 (1939): "No petition can be approved as properly filed under Chapter X until the court has determined that the system of Chapter XI could not provide adequate relief in the situation of the case. This oblique definition of jurisdiction under Chapter X can be evaded at will unless a comparable condition is read into Chapter XI. * * * If petitions under Chapter X are accepted when relief under Chapter XI would be inadequate, petitions under Chapter XI should be rejected for the same reason; and the prospective inadequacy of relief under Chapter XI should be the same question when presented as an issue in Chapter XI proceedings as when it arises at the hearing on the approval of the petition, in a Chapter X proceeding."

sion to intervene in the proceeding is, we believe, clearly erroneous. In effect, the decision establishes the principle that, in the absence of express statutory provision, a governmental agency may never intervene to protect the public from evasion or emasculation of the statute under which the agency functions, unless the agency has some property or pecuniary right affected by the litigation. This drastic restriction upon the power of the Government to protect the public interest finds no support in precedent or policy.

In our view, the approach of the court below was wrong. It pointed out first that Chapter X contains an express provision for Commission intervention while Chapter XI does not, and stated that this "raises a strong implication against intervention by the Commission" in Chapter XI proceedings (R. 423). It then addressed itself to the question of whether the interest of the Commission in the litigation was so direct and immediate as to entitle it to intervene *as of right* and held that, since the Commission did not "stand to gain or lose directly by the decision of the court," it did not have such an interest (R. 424). There is no discussion in the opinion of whether the Commission's interest in the action was such as entitled it to intervene *with the permission of the court.* Apparently the court below failed to realize that, since the District Court granted the Commission's motion to intervene, the question was not only whether it

could intervene as of right, but also whether the District Court's action in allowing it to intervene constituted an abuse of discretion.

The reliance of the court below upon the provision of Chapter X expressly providing for Commission intervention is, we believe, misplaced. The purpose of this provision is obviously to allow the Commission properly to perform the advisory functions with which it is charged in Chapter X proceedings. Since the Commission has no similar functions to perform in Chapter XI proceedings, a provision giving it a general right to participate in ChapterXI proceedings would be both inappropriate and superfluous.

The Commission did not intervene here in order to perform advisory functions, but to object against an improper exercise of the court's jurisdiction which, in the opinion of the Commission, nullifies the protection provided by Congress for investors. Its standing to intervene, therefore, does not depend on the provisions of Chapter XI but upon the broad question whether it had sufficient interest to entitle the judge in charge of the proceeding to allow intervention under the general principles governing intervention in the federal courts.

The answer to this question cannot be in doubt. The interest of the Commission in the proceeding is twofold. First, as the agency designated by Congress to participate in Chapter X proceedings "in the interest of adequate representation of the

public interest,"[29] it has a very definite interest in objecting, if indeed it is not under a duty to object, on behalf of the investing public against an improper exercise of jurisdiction under Chapter XI which deprives investors of the safeguard contained in Chapter X. Second, it has an equally great interest in protecting its own functions under Chapter X from impairment through improper resort to Chapter XI by corporations which should file under Chapter X.[30]

This Court has recognized that public officials and administrative commissions, federal and state, have a legitimate interest in resisting any endeavor to evade the provisions of the statutes in relation to which they have official duties. Cf. *Coleman* v. *Miller*, 307 U. S. 433, 442, 466; *Pennsylvania* v. *Williams*, 294 U. S. 176.[31] The *Williams* case is strikingly similar to the present one. There a re-

[29] S. Rept. No. 1916, 75th Cong., 3d Sess., p. 33.

[30] If the court below were correct in stating that the Commission has no interest to protect until a Chapter X proceeding is pending (R. 423), it would mean that the Commission would never have an opportunity to protest in the interests of the public investors which it represents against an improper resort to Chapter XI which deprived those investors of the protection of Chapter X.

[31] The preservation of governmental functions from impairment through the improper exercise of jurisdiction has frequently been held by state courts to constitute sufficient basis for an action for a writ of prohibition. See, e. g., *State* v. *Superior Court for Walla Walla County*, 159 Wash. 335, 293 P. 986 (1930); *State* v. *Superior Court of Marion County*, 202 Ind. 589, 177 N. E. 322 (1931).

ceivership proceeding was commenced in the federal court. The State of Pennsylvania filed a petition for leave to intervene and for an order directing the receivers to surrender the assets of the defendant association to the State Secretary of Banking for liquidation under the provisions of state law. The District Court denied the petition but this Court reversed, holding that the District Court in the exercise of its discretion should have discharged the receivers and directed the surrender of the property in their possession to the Secretary. The granting of this relief necessarily implied that the state had an interest sufficient to give it standing to intervene.

The majority opinion below attempts to distinguish the *Williams* case on the ground that the state "claimed a right to full possession and control of the assets of the insolvents, not merely a right to advise or protect the public interest" (R. 423–424). The distinction is not substantial. The interest of the state in the receivership proceeding was not a property or possessory interest but an interest in the enforcement of the state liquidation statutes for the protection of the public. That is precisely the type of interest which the Commission has in the present case. That Congress sought to protect the investing public by making the Commission an advisory, rather than a liquidating, agency is immaterial; in each case the administrative body has the same interest in assuring that the

public will receive the protection which the agency was designed to afford it.[32]

The decision of this Court in *The Exchange*, 7 Cranch 116, likewise supports the Commission's position. That case involved a libel filed by American citizens against a schooner which the libellants claimed to be their property. The schooner was, in fact, a French vessel of war in possession of French naval officers, although it was within the waters of the United States. After the libel was filed the United States District Attorney filed a "suggestion" setting forth the facts and praying that the schooner be released.[33] The District Court dismissed the libel, but on appeal the Circuit Court reversed. The District Attorney thereupon appealed to this Court, which reversed the judgment of the Circuit Court and affirmed the judgment of the District Court dismissing the libel. The Court, first expressing the opinion that an American citizen cannot assert, in an American court, title to a

[32] In *State* v. *Superior Court of Marion County*, 202 Ind. 589, 177 N. E. 322 (1931), a state banking commissioner was permitted to intervene in an action for a writ of prohibition to prevent a state court from exercising jurisdiction to appoint a receiver for a state bank at the instance of a creditor. The commissioner neither had nor claimed possession of the assets; his "interest" consisted in the fact that he alone was entitled to ask for a receiver.

[33] Although the opinion in *The Exchange* does not speak of intervention, the procedure followed was the same as intervention, if it was not intervention in fact. This Court so recognized in *Stanley* v. *Schwalby*, 147 U. S. 508, 513.

public armed vessel in the service of a foreign sovereign, added (p. 146): "If this opinion be correct, there seems to be a necessity for admitting that the fact might be disclosed to the court by the suggestion of the attorney for the United States."

The course sanctioned by this Court in *The Exchange* was almost identical with the course pursued by the Commission here. There the United States appeared in the proceedings in order to move their dismissal on the ground that the court had no jurisdiction and that an improper exercise of jurisdiction would be contrary to the public interest; its contentions having been overruled in the circuit court, an appeal was allowed. As pointed out in *Percy Summer Club* v. *Astle*, 110 Fed. 486, 489 (C. C. D. N. H.), *The Exchange* case illustrates that the principle allowing intervention by public authorities where the public interest is concerned "is of the broadest character, and is applied without formalities."[34]

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[34] Other cases in which governmental intervention has been allowed cannot satisfactorily be distinguished on the ground that in those cases a claim of title, a pecuniary interest, or a trustee's interest was involved. Those factors are material as establishing the existence of a public interest; they do not limit the character of the public interest which, when otherwise shown to exist, is sufficient to justify intervention. Cf. *Helvering* v. *Davis*, 301 U. S. 619; *United States* v. *Minnesota*, 270 U. S. 181, 194; *Norman* v. *Consolidated Edison Co. of New York*, 89 F. (2d) 619 (C. C. A. 2d); *Winola Lake & Land Co., Inc.* v. *Gorham*, 17 F. Supp. 75 (M. D. Pa.).

The assumption underlying the decision below that in the absence of statutory provision a governmental agency may not apply to the courts to protect the public interest, as distinguished from its own pecuniary interest, is also directly contrary to the principle enunciated in *In re Debs*, 158 U. S. 564. There the Court upheld the power of the United States to file a bill in equity to enjoin obstruction by the defendant of the interstate transportation of persons and property, as well as of the carriage of the mails; the decision was expressly rested upon the principle that a government entrusted "with powers and duties to be exercised and discharged for the general welfare, has a right to apply to its own courts for any proper assistance in the exercise of the one and the discharge of the other" and that it is immaterial that the government "has no pecuniary interest in the matter" (p. 584). See also *Hopkins Savings Assn.* v. *Cleary*, 296 U. S. 315, 339–341.[35] A nonpecuniary

[35] Cf. *Interstate Commerce Commission* v. *Oregon-Washington R. Co.*, 288 U. S. 14, 25, a suit brought to enjoin an order of the Interstate Commerce Commission, in which the Court held that state utility commissions, which had intervened in the suit, were "aggrieved parties" and therefore had a statutory right of appeal "because they officially represent the interest of their states in obtaining adequate transportation service."

The public interest of a state in the maintenance of transportation facilities has been deemed to give it standing to ask for a writ of prohibition forbidding a circuit judge who had entered a decree of foreclosure to confirm the sale of railroad property as junk. *State* v. *Bullock*, 78 Fla. 321, 82 So. 866, affirmed, 254 U. S. 513.

interest sufficient to support an independent suit for the protection of the public must certainly suffice to support intervention for that purpose in an existing suit. Cf. *New York* v. *New Jersey*, 256 U. S. 296, 307–308.

The general principles of intervention established by the authorities cited are in no way altered or restricted by Rule 24 of the Federal Rules of Civil Procedure, which this Court has ordered to be followed in bankruptcy proceedings "as nearly as may be." General Orders in Bankruptcy, Paragraph 37. The Advisory Committee's Note to Rule 24 specifically states that the rule "amplifies and restates the present federal practice at law and in equity." The Commission may intervene either under clause (a) (2) of Rule 24, which provides for intervention as of right "when the representation of the applicant's interest by existing parties is or may be inadequate and the applicant is or may be bound by a judgment in the action," or under clause (b) (2) which provides for permissive intervention "when an applicant's claim or defense and the main action have a question of law or fact in common."

We submit, therefore, that the Commission had an absolute right to intervene. Its interest in the proceeding is not represented by any other party and that interest will be foreclosed by an adverse judgment, which will effectively prevent the Commission from performing its

functions in relation to the Debtor under Chapter X and will deprive the investors whom the Commission represents of the safeguards provided for them by Congress in Chapter X.[36] Since denial of intervention in the present case would leave the Commission without remedy for the impairment of its functions, the Commission comes within the class of applicants for intervention who "can never obtain relief unless it be granted * * * on intervention in the pending cause. In this latter class the right to intervene is absolute * * *." *United States Trust Co.* v. *Chicago Terminal T. R. Co.*, 188 Fed. 292, 296 (C. C. A. 7th), and cases cited.

But whether or not the Commission had an absolute right to intervene, there can be no question that it was properly permitted to intervene under clause (b) (2) of Rule 24, which merely requires that the intervenor's claim or defense raise a question of law or fact in common with the main action. Here the petition to intervene clearly raised

[36] In *United States* v. *Lane Life Boat Co.*, 25 F. Supp. 410 411 (E. D. N. Y.), it was held that the term "bound" in Rule 24 (a) (2) is not to be strictly construed, even as regards private litigants. Where public agencies are concerned, *Percy Summer Club* v. *Astle*, 110 Fed. 486, 488 (C. C. D. N. H.), indicates that the condition of the rule that the intervenor be bound by the judgment means merely that the practical effect of an adverse judgment must be "prejudicial."

a question of law in common with the main action, since it was addressed directly to the jurisdiction of the court to maintain the main action. And that a motion to dismiss an action constitutes a "defense" to that action within the meaning of the Rule seems plain; Rule 12 (b) expressly provides that the "defense" of lack of jurisdiction over the subject matter may be presented in a responsive pleading or by motion, at the option of the pleader.[37] If it be urged that "defense" refers only to a pleading interposed by one who is technically in the position of the defendant, the short answer is that, so construed, this provision of Rule 24 (b) (2) would not strictly be applicable to anyone seeking to intervene to dismiss a voluntary petition under the Bankruptcy Act, since in such a proceeding no one is ever technically in the position of a defendant. If the Rule is to receive this narrow construction, the result is simply that in a proceeding of this sort the provisions of the Rule may not be applied literally but must rather, as provided by

[37] That the words "claim or defense" were not intended to be construed technically is shown by the remarks of Dean (now Circuit Judge) Charles E. Clark at the proceedings of the American Bar Association Institute at Washington, D. C. In describing Rule 24, Dean Clark, after first stating the requirements for intervention of right, stated that permissive intervention may be allowed in "any other case where a question of law or fact in common with the main suit is presented." See Proceedings of the Institute on Federal Rules at Washington, D. C. (Am. Bar. Assn.), p. 67.

Paragraph 37 of the General Orders in Bankruptcy, be followed "as nearly as may be." Plainly, a motion to dismiss a petition filed under Chapter XI for lack of jurisdiction, made by a party having an interest in the proceeding, is the counterpart in bankruptcy proceedings of a similar motion made in an action at law by one who is technically in the position of a defendant.[38]

2. If the District Court properly exercised its discretion in permitting the Commission to intervene, the Commission had the right to appeal from the orders denying its motions. An interest sufficient to warrant intervention is plainly sufficient to warrant appeal, after intervention, from a decision adverse to that interest. *Pennsylvania* v. *Williams, supra; The Exchange, supra; Texas* v. *Anderson, Clayton & Co.*, 92 F. (2d) 104 (C. C. A. 5th), certiorari denied, 302 U. S. 747. As an intervenor, the Commission was a party and the denial of the relief which it sought made it an aggrieved party. As such, it had the

[38] The principle that intervention must be in subordination to the main action, formerly embodied in Equity Rule 37, has been omitted from Rule 24 of the Rules of Civil Procedure. The omission was deliberate. See remarks of Dean Clark, in Proceedings of the Institute on Federal Rules at Cleveland (Am. Bar Assn.), pp. 265–266. In the absence of an express requirement of subordination, the Commission was clearly entitled to the relief sought if it was properly permitted to intervene and its position is correct on the merits. *Sage* v. *Central R. R. Co.*, 93 U. S. 412.

right, under Sections 24 and 25 of the Bankruptcy Act, to take an appeal. Cf. *Interstate Commerce Commission* v. *Oregon-Washington R. Co.*, 288 U. S. 14, 24–25; *Williams* v. *Morgan*, 111 U. S. 684, 696–698; *Savannah* v. *Jesup*, 106 U. S. 563; *Ex parte Jordan*, 94 U. S. 248; *Sage* v. *Central R. R. Co.*, 93 U. S. 412, 419.[39]

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[39] *Marshall* v. *Dye*, 231 U. S. 250, cited by the court below (R. 424) is not opposed to this conclusion. That case merely holds that those who seek review of this Court of the judgment *of a state court* must have a personal as distinguished from an official interest in the relief sought and in the federal right alleged to have been denied by the judgment of the state court. The decision is clearly inapplicable to proceedings in the federal courts because the basis for the rule enunciated was that the petitioner, "having sought the advice of the courts of his own State in his official capacity, should be content to abide by their decision" (231 U. S. at 258). It should also be noted that the decision was held to be inapplicable to the situation presented in *Coleman* v. *Miller*, 307 U. S. 433, 438.

Chicago v. *Chicago Rapid Transit Co.*, 284 U. S. 577, relied upon by respondent, is also inapplicable. That was a suit brought to restrain the Illinois Commerce Commission and the Attorney General of that state from enforcing an order of the Commission prescribing rates of fare upon the plaintiff's railroads. The City of Chicago was permitted to intervene as a defendant. A three-judge District Court granted an injunction and the Commission and Attorney General decided not to appeal. This Court, in a *per curiam* opinion, dismissed an appeal taken by the City of Chicago on the ground that it had no separate standing to appeal. The decision is not authority against the general proposition that an intervenor is a party entitled to appeal from an adverse order. The authorities cited in the opinion in-

The fact, adverted to by the court below, that Section 208 of the Act prohibits appeals by the Commission in Chapter X proceedings, does not, directly or by implication, limit the Commission's right to appeal in this case. The restriction imposed by Secton 208 was designed to emphasize the advisory nature of the Commission's functions under Chapter X and the ultimate judicial character of the proceedings (see dissenting opinion of Clark, J., at R. 429). The restriction does not in terms apply to the present case, since this is a Chapter XI rather than a Chapter X proceeding, and the policy reflected by the restriction is likewise inapplicable. The appeal was not taken by the Commission from the confirmation of a plan which it did not deem fair and equitable, but rather from an improper exercise of jurisdiction, based on a vital point of statutory construction, which, in the opinion of the Commission, precludes it from performing the functions vested in it by Chapter X and thereby defeats the public interest which the Commission is directed to protect.

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dicate that the basis of the decision was that the regulatory commission, whose order was enjoined and who did not see fit to appeal, rather than the City, was the proper party to determine whether the interests of the public called for review of the decision. The situation here, of course, is not comparable since the Securities and Exchange Commission was the only party in a position to represent the public who could appeal from the decision of the District Court.

CONCLUSION

The judgment of the court below should be reversed and the proceeding remanded to the District Court with instructions to dismiss the Debtor's petition.

Respectfully submitted.

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APPENDIX

Comparison of provisions of Chapter X and Chapter XI

	Chapter X	Chapter XI
1. Initiation of proceeding.	Debtor, three creditors, or indenture trustee may file petition (Sec. 126).	*Only* debtor may file petition (Secs. 321, 322).
2. Appointment of trustee.	Trustee appointed in every case in which indebtedness is $250,000 or more (Sec. 156).	*No comparable provision.* If trustee in bankruptcy has already been appointed, he must be continued in possession. Otherwise, receiver may be appointed "if necessary" (Secs. 332, 343).
3. Qualifications of trustee.	Must be independent, disinterested (Secs. 156, 158).	*No comparable provision.*
4. Examination of Debtor's financial problems and causes of failure.	Trustee investigates property, liabilities, and financial condition of debtor, the operation of the business, and the desirability of its continuance (Sec. 167 (5); *cf.* Sec. 167 (1)).	*No comparable provision.*
5. Report to judge upon past conduct of the Debtor.	Trustee reports to judge facts pertaining to fraud, misconduct, mismanagement and irregularities, and any causes of action available to estate (Sec. 167 (3)).	*No comparable provision.*
6. Reports to security holders.	Trustee submits statement of his investigation to security holders (Sec. 167 (5)).	*No comparable provision.*
7. Formulation of plan.	Trustee gives notice to security holders that they may submit to him suggestions for formulation of plan (Sec. 167 (6)).	*No comparable provision.*
8. Proposal and filing of plan.	Trustee prepares and files plan (or report of reasons why plan cannot be effected) *before* debtor may propose plans or amendments (Sec. 169).	*Only* debtor may propose arrangement (Sec. 323) or modifications (Sec. 363).
9. Assistance of administrative agency.	In cases in which the scheduled indebtedness exceeds $3,000,000, and in other cases if the judge desires, plans which the judge finds worthy of consideration, after hearing, are submitted to the Securities and Exchange Commission for examination and report (Secs. 172, 173). Commission may, with approval of judge, participate in proceeding as a party (Sec. 208).	*No comparable provisions.*
10. Submission of plans for acceptances.	*After* approval by the judge as fair and equitable and feasible, plans are transmitted to security holders together with informative materials, including the judge's opinion and the Commission's report (Secs. 174, 175).	*No comparable provision.*

	Chapter X	Chapter XI
11. Solicitation of acceptances.	May not normally be solicited until *after* judge has approved plan and informative materials have been transmitted (Sec. 179).	May be solicited at any time, even prior to institution of proceeding, and must be obtained *before* court confirms arrangement (Secs. 336 (4), 361, 362). No requirement as to data which must accompany solicitation.
12. Acceptances required for confirmation.	Two-thirds in amount of each affected class of creditors and majority of holders of stock (if debtor is not insolvent) (Sec. 179).	Majority in amount and number of each affected class of unsecured creditors (Sec. 362 (1)).
13. Dissenting classes of creditors or stockholders.	If a class of creditors does not accept by two-thirds in amount, or if a class of stockholders does not accept by a majority, the plan may be confirmed if it provides for such classes adequate protection as prescribed by the statute (Secs. 216 (7), (8), 179, 221).	*No comparable provisions.*
14. Classes of security holders which plan may affect.	Plan may alter and modify the rights of any class of creditors, secured or unsecured, and of any class of stockholders (Sec. 216).	Arrangement may provide for settlement, satisfaction, or extension of unsecured debts only (Secs. 306 (1), 357).
15. Participation in proceeding by security holders.	Have right to be heard on all matters arising in proceeding (Sec. 206); and may act in person, by attorney, or by agent or committee (Sec. 209).	*No comparable provision.* One creditors' committee may be elected at first meeting of creditors (Sec. 338).
16. Control over representatives of security holders.	Information furnished to court concerning employment and interests of representatives of security holders (such as committees, indenture trustees and attorneys), as well as interests of the persons represented (Secs. 210, 211). The judge is empowered to disregard provisions in authorizations of such representatives or to restrain the exercise of powers which are unfair or contrary to public policy (Sec. 212). Claims or stock acquired by the respresentatives in contemplation of or during the course of proceeding may be limited to actual consideration paid therefor (Sec. 212).	*No comparable provisions.*
17. Indenture trustees.	Have the right to be heard on all matters arising in the proceeding (Sec. 206); to file a claim on behalf of all holders of securities outstanding under their indenture (Sec. 198); and to file a petition initiating the proceeding under the chapter (Sec. 126).	*No comparable provisions* and no mention of indenture trustees.

	Chapter X	Chapter XI
18. Lists of security holders.	Trustee is under a duty to prepare and file lists of security holders (Sec. 164). Other persons in possession or control of such lists or information relevant thereto may be required to disclose the lists or such information (Sec. 165). Although in a proper case the court may direct impounding of the lists, bona fide security holders and indenture trustees have an unqualified right to use and inspect them upon terms prescribed by the court (Sec. 166).	*No comparable provisions.* Debtor files bankruptcy schedules with petition (Sec. 324).
19. Compensation and allowances.	In addition to allowances to officers of the court, the debtor and petitioners, the judge has broad power to make reasonable allowances of compensation and reimbursement for expenses to the representatives of security holders, including committees and indenture trustees, and to individual creditors and stockholders and their attorneys. (Secs. 241-242.)	The debtor is required to deposit the money necessary "to pay the costs and expenses of the proceedings and the actual and necessary *expenses* incurred in connection with the proceedings and the arrangement by *the* committee of creditors and the attorneys and agents of such committee, in such amount as the court may allow" (Sec. 337 (2).)
20. Subsidiary corporations.	A petition by or against a subsidiary corporation may be filed in the same court which has approved the petition by or against the parent corporation. (Secs. 129, 106 (13).)	*No comparable provision*, and no mention of subsidiaries.
21. Future management.	Plan must contain provisions which are equitable, compatible with the interests of security holders, and consistent with public policy, with respect to the manner of selection of the reorganized company's directors and officers (Sec. 216 (11)); and identity, qualifications, and affiliations of the persons to be directors and officers must be disclosed and meet same test. (Sec. 221 (5).)	*No comparable provision.*
22. Charter of reorganized company.	Plan must contain provisions requiring inclusion in the reorganized company's charter of provisions for the prohibition of the issuance of nonvoting stock, for the equitable distribution of voting power among the new securities possessing such power, for the election of directors representing preferred stockholders in the event of default in payment of preferred dividends, for the general fair and equitable treatment of securities, and for periodic corporate reports to security holders (Secs. 216 (12)).	*No comparable provision.*

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